UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK
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SECURITY INSURANCE COMPANY OF HARTFORD,

Plaintiff,

v. 07 CV 3277 (VM)

COMMERCIAL RISK REINSURANCE COMPANY, LTD.,

Defendant.

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New York, N.Y.
May 8, 2007
10:40 a.m.

Before:

HON. VICTOR MARRERO,

District Judge

APPEARANCES

STROOCK & STROOCK & LAVAN
Attorneys for Plaintiff
BY: MICHELE L. JACOBSON
REGAN A. SHULMAN
CHRISTIAN FLETCHER

D'AMATO & LYNCH
Attorneys for Defendant
BY: JOHN P. HIGGINS
EDWARD M. ROTH
-AND-
LAW OFFICES OF DAVID L. FERSTENDIG
BY: DAVID L. FERSTENDIG

(In open court)

(Case called)

THE COURT: This is a proceeding in the matter of Security Insurance Company v. Commercial Risk Reinsurance Company, docket number 07 CV 3277.

The Court has before it plaintiff's motion and petition to compel arbitration. The parties have submitted briefings on the issue; the matter is fully briefed. And the Court scheduled this proceeding to hear whatever additional points the parties may wish to stress for the record beyond what is already in the papers that the Court has thus reviewed.

In particular, the Court believes that the basic question is on what grounds should there be the reconstituting of a panel that is requested by defendants under these circumstances.

For the plaintiffs, who speaks, Ms. Jacobson?

MS. JACOBSON: Yes, your Honor.

THE COURT: Yes.

MS. JACOBSON: We represent the petitioner in this proceeding. We believe that the respondent's admissions in this case is set forth in their answer to the petition, as well as the parties' agreement and the case law all establish that what the respondents are seeking to do here, reconstituting the panel, is completely without basis; and that, in fact, the parties' agreement and the case law demonstrates that the

petition to compel arbitration should be granted.

In particular, I want to point out several of the facts which are admitted.

First, respondents have admitted that there is an agreement to arbitrate. Second, the respondents agree that the parties selected Mr. David Thirkill as the umpire; and that the defendants have agreed that prior to Mr. Dielmann's resignation, the parties agreed to proceed with the non-DIG arbitration during the week of June 25th. And they admit that they have refused to proceed with the proceeding on June 25th with the designated umpire.

Now, I think it's important to take a look at the parties' arbitration agreement. And that is set forth at Exhibit 1 to my declaration.

Under the arbitration provision, which is located on page 18 of Exhibit No. 1, it plainly states that the parties each select their own arbitrator, and together those arbitrators select a third arbitrator whom the parties in this matter have called the umpire. And I'm, frankly, mystified that the respondents would argue that Mr. Thirkill was the umpire, because if you would note, attached to Exhibit 1 of my reply declaration is the cover of their position statement noting that Mr. Thirkill is the umpire.

But, at any rate, if we go further into the provision, it says that, The parties hereby waive all objections to the

method of the selection of the arbitrators; it being the intention of both sides that the arbitrators be chosen from those submitted by the parties. So once an arbitrator is selected, you can't complain about how they were selected. And importantly, if we look a little further up in the provision, it states that the hearing is to take place within 30 days of the appointment of a third arbitrator.

Now, the parties agree to modify this provision to require that the hearing take place on the week of June 25th. So that is the amendment to this provision. We have an agreement to arbitrate on June 25th. And Security Insurance Company of Hartford has not not agreed to amend that change.

So what we have here is we have the fact that there can be no challenges to the method of umpire selection, and we have contractually-agreed-upon dates. That comes out of the parties' arbitration provision.

Now, Commercial Risk, the respondents here, are claiming that they can use the resignation of their party-appointed arbitrator to essentially bring this arbitration back to its inception as though that umpire selection had never occurred, as though the parties had never given hold-harmless agreements to the entire panel and agreed to the selection of the panel.

They claim that it's unfortunate that their arbitrator resigned; but, however, what they are doing is they are

attempting to use that to their advantage. They are attempting to take the resignation of their arbitrator and use it as a means to displace the umpire who was chosen by both of the parties, but who had previously ruled against them in the DIG arbitration.

Now, how did they find support for their claim? Well, I would submit there is none. They cite what is called a general rule on panel vacancies. But the rule that's expressed by the Second Circuit in the *Marine Products* case was two faceted: First off, the arbitrator died. And most importantly, the matter was what's called *in medias res*, in the heart of the matter.

In *Marine Products*, the party arbitrator died after there had been an evidentiary hearing at which a very important witness had testified. There had been submission of evidence to the panel, and there had been additional interlocutory rulings. In that case, coming up on a motion to vacate, the Second Circuit said, We're not going to vacate the district court's order reconstituting the panel where the matter was *in medias res*.

Now, the *Trade and Transport* case, also decided by the Second Circuit, said, Well, wait a minute. It's not an automatic that you reconstitute the entire panel when an arbitrator dies. You have to look to see whether or not there are special circumstances, including the parties' agreement,

and also including the procedural posture of the case.

And in *Trade and Transport*, where there was nothing currently pending before the panel, the Court ordered a replacement arbitrator. And specifically, the Second Circuit said that, in essence, there would be no need to filling a vacancy, the language "filling a vacancy" in Section 5 of the FAA. It would, "make no sense if the act were construed to require that whenever one arbitrator died, the entire panel must be removed." And that is at 196 of the *Trade and Transport* case.

So in that situation, since there was nothing currently pending before the arbitration panel, the Court found that replacement, not complete going back to day one, was required.

We are very similar to the posture in *Trade and Transport*. Nothing is pending currently before the panel. There was an organization meeting over a year ago. There was an order of prehearing security that was entered by the panel. Now, that order of prehearing security is a final order of the panel, not revisited.

Under the *Banco de Seguros v. Mutual Marine* case, the Second Circuit 2003, the Second Circuit held that an award of prehearing security is the final order of the panel such that you could move to vacate it.

So we are in a similar situation to *Trade and*

Transport where there had been an order, a final order, issued by the panel, but nothing currently pending.

Now, frankly, we are on all fours. We are very close to the *Trade and Transport* situation. We are not at all in the situation of the *Marine Products* case where right in the middle of evidence being heard. We have none of that here.

Defendants also cite to the *Pemex* case. They claim that the facts of that case show that the panel had issued a procedural ruling. That's completely untrue. The *Pemex* case, the facts are clear that the entire evidence had been submitted before the arbitration panel, all documentary evidence, all testimony, and, in fact, what was going on was post-hearing briefing when the arbitrator died.

So we don't believe that the general rule, to the extent that there is one, should apply in this instance. And that what is required, we believe, is the replacement of the one arbitrator who resigned.

Now, I don't think that there's a doubt that we had a panel vacancy. Your Honor can appoint a replacement under Sections 5 and 206 of Title 9. We contend that there is a lapse because the court-appointed arbitrator which they have selected has refused to disclose whether or not he's disinterested. And we asked him to make those disclosures a month ago. He has not disclosed whether he's disinterested. And Commercial Risk has stated nothing in their papers which

would inform us or your Honor whether or not he is, in fact, disinterested or whether or not he's available to appear as arbitrator on the June 25th hearing date.

I want to make it clear that if Mr. Gentile is, in fact, disinterested, we are prepared to proceed before Mr. Gentile, Mr. Thirkill, and Mr. Haber on June 25th. However, if they are unwilling or unable to make representations concerning his disinterestedness or his availability to your Honor, we would ask that your Honor order a replacement arbitrator. Thank you.

THE COURT: Thank you. Mr. Higgins?

MR. HIGGINS: Thank you, your Honor. I'd like to start by talking about what the Arbitration Act provides so that we can narrow the scope of the discussion.

The courts have avoided and the legislature obviously, Congress obviously, avoided the issue of the judge or the courts getting involved in the details of an arbitration. There is provision for an order to arbitrate. There's no provision allowing a court to get involved when an arbitration takes place, how an arbitration takes place, where an arbitration takes place, and that sort of thing. Witnesses, evidence, those are left for the arbitrators. And in this case, procedures by virtue of the agreement are left to the arbitrators. So we can start with the idea that no matter who the panel is that this proceeds before, it's for the panel to

decide how it goes forward.

Now, reverting to the issue, it seems to us kind of odd that we would be dealing with allegations of manipulation throughout the whole process, and then at this argument we deal with case law, which is what we intended to try to focus on from the beginning.

As the Court knows, we are faced with quite a bit of material which made allegations of wrongdoing by our firm, by our clients, and by the arbitrator who resigned. An expert affidavit was put in basically which parroted those allegations. They talked about the catastrophe that this process would have on reinsurance arbitrations. The implication, more than an implication, we would say, is that the resignation was a manipulation; was, in essence, a conspiracy; that we directed it. Those words are used in the expert conspiracy-ism, but that counsel directed it.

This obviously is not something that we believe the courts should allow, tossing around these wild unsubstantiated allegations, and then backing away, but not backing away. Even in the argument this morning, the statement was made that the reason we want to go through this process is because there was an unfavorable ruling in the other arbitration. That obviously is irrelevant, unless there's a reason why it would be relevant. And the only reason it could be relevant is if we created the situation. And we believe that we are entitled to

a hearing on the facts and circumstances of the resignation so that we can establish that this is not a case where the resignation was caused by or agreed with an arbitrator for an ulterior improper purpose.

And we are advised, assured, actually, that the arbitrator, T. O. Dielmann, will come to this country, and will testify. Actually, he's anxious to testify to clear his name, really, after having been accused of the things he's been accused of, not only by Security Insurance, but also by the expert that's submitted the affidavit.

Now, these documents have not been withdrawn, so we have to assume that they are still part of the record, because Security Insurance expects the Court to rely on them. And we believe that we should be able to put in evidence to prove the facts and to show how we got here and why we got here.

Now, turning to the law. A statement was made that the general rule, and I think it's a quote, to the extent that there is a general rule -- well, that's not accurate. There is a general rule. And it's repeated in *Trade and Transport*. There was a general rule before that, because obviously they are not making a rule, they are stating the existence of a rule. The rule is modified in some instances where there are special circumstances. None of the cases cited have any circumstance anywhere near what we have here. Cases where you have a bifurcation, you have a ruling on the first issue, is

obviously not apt, not pertinent to this case here. We don't have any final rulings on material issues going to the merits.

Here, there is really no difference in terms of special circumstances between going ahead in one fashion or the other. There hasn't been any statement as to why there's any proprietary interest as it were in proceeding with the two arbitrators that remain.

If a third arbitrator is selected now, presumably neutral, it won't cause any material delay. Nothing's really been done other than some discovery, which obviously wouldn't be redone. It would take very little time for a new arbitrator to educate himself, no more than it would take the arbitrator that we have appointed to educate himself.

THE COURT: Mr. Higgins, you are addressing the questions of what would not happen. But address the question of what prejudice there is to you for the process to proceed at this point. What is to be lost?

MR. HIGGINS: What is to be lost with what, your Honor? I'm sorry.

THE COURT: With proceeding from where we are now, as opposed to starting all over again with the designation of new arbitrators; replacing the arbitrator who resigned and moving along as opposed to starting all over again.

MR. HIGGINS: The prejudice to us?

THE COURT: Yes.

MR. HIGGINS: The prejudice to us is that we wouldn't be entitled to what we are entitled to under case law, which is selection of a new panel. If we are entitled to that right, we want to enforce that right.

THE COURT: All right. So that assumes your reading of the case law.

MR. HIGGINS: Yes.

THE COURT: All right.

MR. HIGGINS: And if we are not entitled to it, then so be it. We allege and we assert that the case law, the general rule, applies here; and there is no exception which fits these facts.

And we also ask for a hearing on the facts and circumstances of the withdrawal which Security Insurance has alleged is material under *Trade and Transport*. And that being the case, we would like to establish the material facts associated with that withdrawal.

THE COURT: All right. Thank you.

MS. JACOBSON: Your Honor, may I respond?

THE COURT: Quickly.

MS. JACOBSON: Yes, your Honor. I want to clear the record. We certainly did not make any allegations in our papers as to the precise reasons for the withdrawal. When we received the e-mail from Mr. Dielmann stating that he was withdrawing, he noted in his e-mail that it had been after

in-depth deliberation.

When we made inquiry of Mr. Higgins as to whether or not there had been communications with Mr. Dielmann in light of that language in the e-mail, they wrote back and they said we're not telling you anything. And those are the facts as we set them out in the brief. There were no accusations.

Now that we have the representation that Commercial Risk nor Mr. Higgins' firm asked Mr. Dielmann to resign, we're satisfied with that. But we believe that the fact that they did not respond to us when we asked the question in setting that out in a factual format, to the extent that there are negative inferences to be drawn from that, I can't help that. The facts are what the facts are.

With respect to the contention that they are entitled to a hearing, I would point the Court to *Interocean Shipping Company v. National Shipping and Trading Corporation,* 462 F.2d 673 (2d Cir. 1972). The Court held there that in order to have a hearing with respect to a motion to compel arbitration, the proponent of the hearing has to have an unequivocal denial that the agreement to arbitrate had been made. And here, there is no unequivocal disagreement that there is an arbitration agreement here. So under the *Interocean* case, your Honor, no hearing is necessary. Your Honor is free to rule. Thank you.

THE COURT: Thank you.

MS. JACOBSON: Oh, and one item further, your Honor.

We would ask that you retain jurisdiction of this matter following your Honor's rulings. Thank you.

THE COURT: All right. Thank you. Yes, Mr. Higgins?

MR. HIGGINS: Just a couple of really quick points. The statute talks about two things; one is the existence of the agreement to arbitrate, and the other is whether a party is in default.

We have appointed an arbitrator. We have asked him to contact the other arbitrator under the arbitration agreement and proceed. We take the position we're not in default. That obviously is a question of fact, as well perhaps is a question of law. And we think that entitles us to a hearing so long as the circumstances of the withdrawal are material to the issue.

On the other point, in terms of deliberation, we didn't really understand the implication that was trying to be made from that. So we looked up the word in the dictionary? Deliberation doesn't require two people. Mr. Dielmann indicated that he had deliberated, and we would like to bring him here and have him testify as to all the circumstances of his deliberation. We certainly don't recognize a right of counsel to demand of us anything in connection with our communications with Mr. Dielmann. If they have a right to question Mr. Dielmann, they can direct their communications with him.

THE COURT: All right. Thank you. I've reviewed the

papers sufficiently and heard the arguments. I am persuaded that plaintiffs are entitled to an order to compel arbitration. I think the record is clear that there is an agreement here to arbitrate in accordance with the schedule that had been set forth for June 25th. There is no indication on the record that that agreement or that schedule had been modified in any way mutually.

I believe that the resignation of the respondent's arbitrator under these circumstances does not give rise to a requirement that the entire panel be reconstituted under these circumstances.

I don't believe this case falls under the rule of *Marine Products*; and that it falls more closely into the circumstances in *Trade and Transport*.

The fact that in *Marine Products* there had been proceedings already on the way, evidence taken, and substantial progress towards the resolution or adjudication on the merits is not a fact here, and there's nothing in the record to indicate that this process had gone far enough to cause any form of prejudice by having the replacement of one arbitrator who has resigned. I don't see those circumstances present here.

I do not believe that the rule that the respondents claim they are entitled to applies in this case. I read the rule to suggest rather that because there have not been any

material progress or proceedings towards addressing the merits or evidence taken on any other major procedural steps, that would have caused prejudice if the proceeding continued under the same arbitrators as present here.

I also do not believe that a hearing here to go into the facts and circumstances of the resignation are indicated. I don't see that that's material to the issue of whether the process should not proceed with simply by the designation of a new arbitrator by the respondents.

The proceedings should continue as scheduled with the respondents designating a substitute. And if the person who is designated for any reason is not prepared to indicate disinterest in this, perhaps that issue could be revisited here; but short of that, I am going to order that the proceedings continue as scheduled pursuant to the parties' agreement.

Is there anything else, Ms. Jacobson?

MS. JACOBSON: I just repeat our request, if your Honor would retain jurisdiction over this matter.

THE COURT: For what purpose, Ms. Jacobson?

MS. JACOBSON: For any further issues that could arise as a result of the arbitration moving forward, as well as to confirm an arbitration award that may be later rendered by the panel.

THE COURT: Mr. Higgins?

MR. HIGGINS: Yes. We would oppose retaining jurisdiction for other than the possibility of enforcing an award. We don't see anything about the Court's award which is non-final at the moment.

THE COURT: Well, I'll consider that issue. The Court believes the granting of the relief here, which is order compelling arbitration, is a final award. If there's any reason why that order needs to be reopened, Ms. Jacobson, you could just address whatever the circumstances may be and I'll take it into consideration.

MS. JACOBSON: Okay. Thank you, your Honor.

THE COURT: All right. Thank you.

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